



# Inn Valuation Essentials

*Please be respectful of your colleagues by silencing your phone. If you need to answer a call, please go to the hallway.*





## What is Value?



### Price

Asking or selling  
One person's  
assessment of  
value



### Cost

Actual amount  
paid or actual cost  
to build or improve



Value is defined as  
*the power of a  
good or service to  
command other  
goods or services  
when exchanged  
in the  
marketplace.*

# Types of Value



## Investment value

The value to a specific investor based on that investor's requirements



## Insurable value

The value of those parts that are physically destructible



## Assessed value

Value established by a tax assessor



## Liquidation value

The likely price that could be realized is a forced sale



## Fair Market Value (FMV)



# Fair Market Value

---



*The most probable price a property would bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus. (The Appraisal Foundation)*



Both parties motivated, informed, acting in own self-interest

Reasonable time for market exposure

Payment in cash (not goats or shells!)

No unusual financing concessions



**The value used for loan underwriting purposes**



## Key Value Considerations



**What is “highest and best use?”**

Residential or commercial?

Depends on the property and the party



**Highest and best use can be affected by improvements**

Positive and Negative!

Understand what you are buying or selling, and know what its true value is

## Some Definitions

**“Financially Viable”** means inns and B&B’s that generate sufficient income to cover operating expenses, debt service (mortgage), and owner’s compensation.

**“Feasible”** means properties with a size and location that have the realistic potential to become financially viable. They may include unique hospitality properties that are distressed, closed, under-performing, or currently used for other purposes.

**“Lifestyle”** means inns and B&B’s whose smaller size and revenues may not generate sufficient income to cover operating expenses and debt service (mortgage). These inns are priced primarily on real estate value.



# Common Valuation Methods for Inns and B&B's



Gross Revenue Multiplier (GRM)



Price per Room (PPR)



Cost / Asset Approach



Capitalization Rate (cap rate)



Financial and investment analysis



Combination of all of the above

Small B&Bs affected by local real estate values

Larger inns affected more by cash flow; have a more national marketplace

$$E\left(e^{\frac{\eta}{\beta}}\right) = \frac{\pi}{\beta * \sin \frac{\pi}{\beta}}, \text{ en el modelo logit}$$

$$E\left(e^{\frac{\eta}{\beta}}\right) = e^{\frac{1}{2\beta^2}}, \text{ en el modelo probit}$$



## \*\*\*!!! IMPORTANT LESSON !!!\*\*\*

01

GROSS REVENUE IS THE TOTAL REVENUE COMING INTO THE BUSINESS FROM ALL SOURCES (ROOMS, EVENTS, FOOD & BEVERAGE, GIFT SHOP, ETC.)

02

NOI (NET OPERATING INCOME) IS THE PROFIT AFTER DEDUCTING OPERATING EXPENSES BUT BEFORE DEBT SERVICE, OWNER COMPENSATION, DEPRECIATION, ETC. (EBITDA)

03

NOI IS THE AMOUNT AVAILABLE FOR A BUYER TO PAY DEBT SERVICE AND TO PAY THEMSELVES.



## Using the Tools: GRM

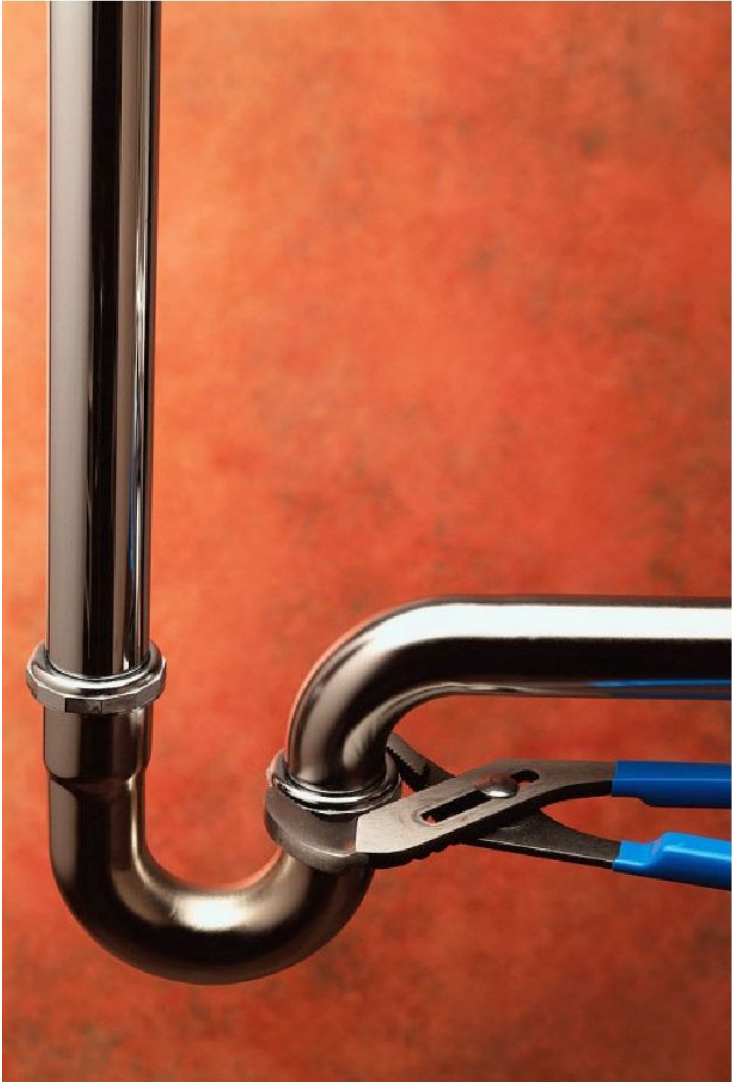
---

- GRM = Gross Revenue Multiplier
  - Sale or asking price  $\div$  gross revenues = GRM
  - Price is \$1,000,000 and room revenues are \$200,000
  - $\$1,000,000 \div \$200,000 = 5.0$  GRM
- Or the other way:
  - Revenues are \$200,000
  - Comparable GRM is 5.5
  - $\$200,000 \times 5.5 = \$1,100,000$
- GRM can range from 2-10 or higher; 4-6 (on *room* revenues) for financially viable B&Bs; lower with food service
- Does not consider condition, owner's quarters, land, other amenities



## Using the Tools: PPR

- PPR = Price Per Room
  - Sale or asking price  $\div$  number of rooms = price per room
  - Price is \$1,000,000; 10 rooms
  - $\$1,000,000 \div 10 = \$100,000$  per room
- Or, comparable PPR x number of rooms suggests a price
  - 10 rooms; comparable PPR is \$150,000
  - $10 \times \$150,000 = \$1,500,000$
- Crude, unreliable tool for inns and B&Bs, which are all unique. Works well for hotels / motels



## Using the Tools: Cost / Asset Approach

---

Reliable tool for lifestyle B&B's that considers most valuable asset first

Value of real estate (as residence) plus one year's gross *room* revenue if revenues exceed value of trade fixtures (FF&E = furniture, fixtures, & equipment)

Real estate worth \$500,000. FF&E worth \$50,000. Gross revenues = \$75,000.

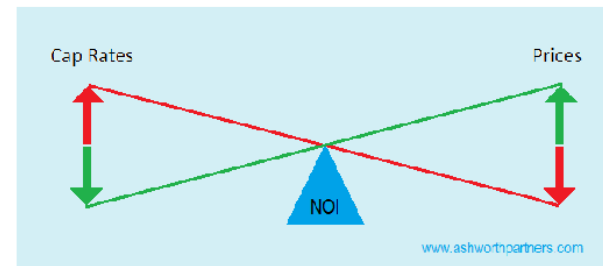
Revenues exceed value of FF&E.  $\$500,000 + \$75,000 = \$575,000$

## Using the Tools: Cap Rate



- Best quick tool to assess value and ability to finance a financially viable inn.
- Capitalization rates (on room revenue) for financially viable inns range 8-11%. Can go higher with restaurant.
- Capitalization rate calculated by dividing NOI (net operating income) by the price, as a %

# Cap Rate Example



- Gross revenue = \$225,000; operating expenses = \$125,000;  
NOI = \$100,000
- $\text{NOI} \div \text{cap rate} = \text{price (value?)}$
- Cap rates and price are inverse
  - $\$100,000 \div 9\% \text{ cap rate } (.09) = \$1,111,111$
  - $\$100,000 \div 10\% \text{ cap rate } (.10) = \$1,000,000$
  - $\$100,000 \div 11\% \text{ cap rate } (.11) = \$909,091$
- $\text{NOI} \div \text{price} = \text{cap rate}$

# Financial / Investment Analysis

**Business Analysis**

Revenue	Profit	Gross Profit	Net Profit
\$100,000	\$20,000	\$80,000	\$10,000
\$200,000	\$40,000	\$160,000	\$20,000
\$300,000	\$60,000	\$240,000	\$30,000
\$400,000	\$80,000	\$320,000	\$40,000
\$500,000	\$100,000	\$400,000	\$50,000
\$600,000	\$120,000	\$480,000	\$60,000
\$700,000	\$140,000	\$560,000	\$70,000
\$800,000	\$160,000	\$640,000	\$80,000
\$900,000	\$180,000	\$720,000	\$90,000
\$1,000,000	\$200,000	\$800,000	\$100,000

### Detailed asset analysis of the physical plant

Detailed financial analysis of occupancy, profit and loss

### Detailed investment analysis

Can the inn pay for itself? Will a bank finance it?

Only works for  
some inns





# Use the Whole Toolbox

---



Similarities  
between valuation  
methods suggest a  
solid valuation



Differences require  
interpretation



Sometimes  
differences can be  
averaged



Some methods  
may have to be  
discounted

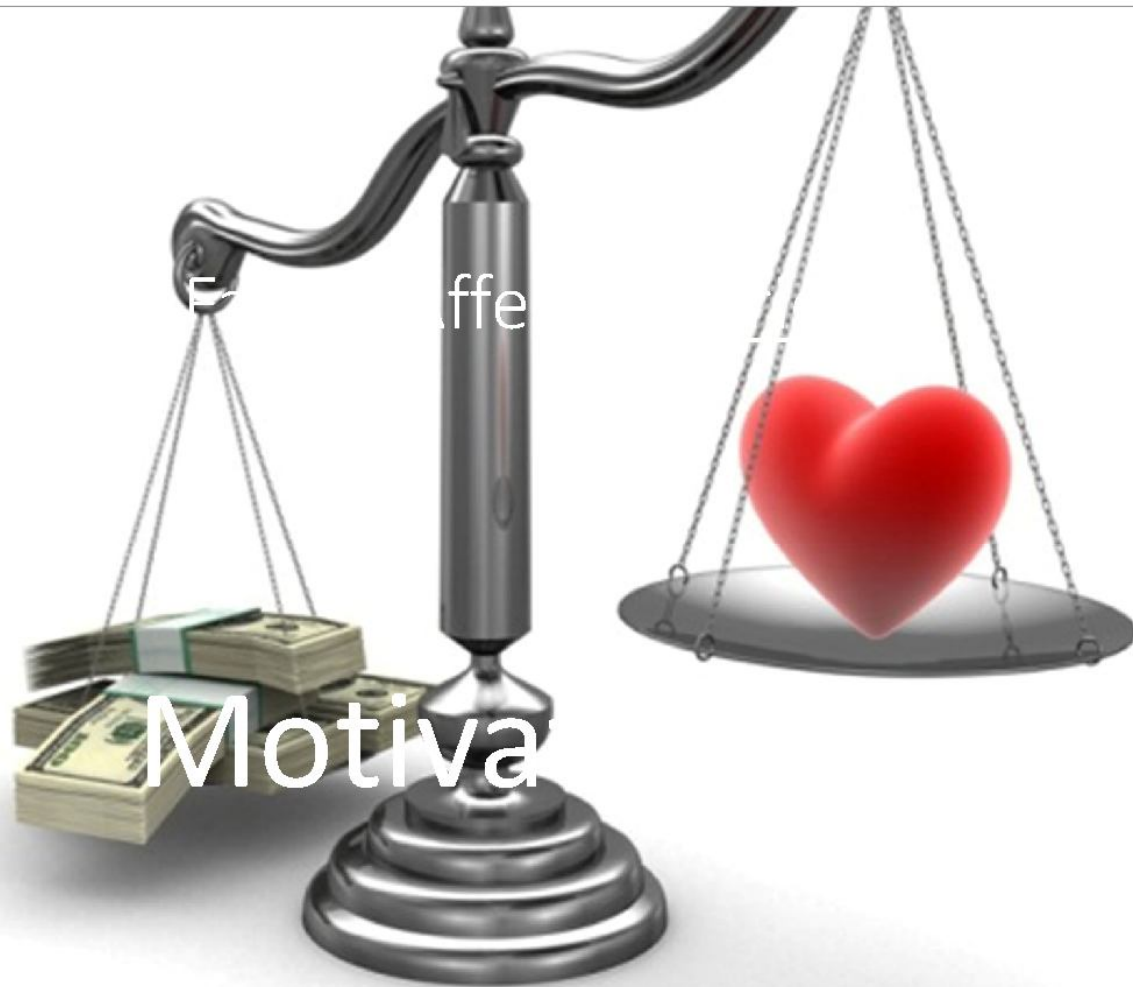


**DON'T  
GUESS!!!**

## Key Factors Affecting Value

- **Location**
- **Condition**
- **Income**





Effort

Motivation

## Key Factor Affecting Sale



Price

Get it right the first time,  
and the rest will fall into  
place!



*Inn Consultants and Brokers Since 1993*

*[www.bbteam.com](http://www.bbteam.com)*

Peter Scherman and Rick Wolf

Thank you for learning with us! Please complete your evaluation and hand it to the room host before leaving the room!